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IN THE

Supreme Court of the United States

OCTOBER TERM, 1947

NO. 540

ESTATE OF CHARLES M. THORP, Deceased, GOLDIE D. THORP and FIDELITY TRUST COMPANY, Executors, Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT AND BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

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COMMISSIONER OF INTERNAL REVENUE, Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

To the Honorable Fred M. Vinson, Chief Justice of the United States, and the Associate Justices of the Supreme Court of the United States:

The petitioners respectfully pray that a writ of certiorari issue to review a decision of the United States Circuit Court of Appeals for the Third Circuit, entered December 2, 1947, affirming a decision of the Tax Court of the United States entered November 21, 1946.

SUMMARY STATEMENT OF THE MATTER INVOLVED.

A. The Proceedings Below.

The Opinion of the Tax Court of the United States was entered on November 21, 1946, and is reported in 7 T. C. 921. The Opinion of the Circuit Court of Appeals was entered on December 2, 1947, and is not yet officially reported. A certified copy of petitioners' Appendix and proceedings in the Circuit Court of Appeals for the Third Circuit, including the Opinion of the Court, is filed herewith.

B. The Facts of the Case.

This petition seeks a review of a decision of the Circuit Court of Appeals for the Third Circuit affirming a decision of the Tax Court of the United States, which re-determined a deficiency in Federal Estate Tax of the Estate of Charles M. Thorp, deceased, in the gross amount of $103,417.12. (App. 28 a) For convenience, Charles M. Thorp is referred to hereinafter as the "decedent." His death occurred on December 14, 1942. (App. 14 a)

The alleged deficiency arises out of the determination by the Commissioner of Internal Revenue that there should be included in decedent's gross estate, for Federal Estate Tax purposes, the value of certain remainder interests under a trust created by decedent in the year 1918. Such determination was made on the ground that a reservation by decedent of a so-called "power of termination" of the trust, required the inclusion of the value of such remainder interests in the decedent's

gross estate under Section 811(d)(2) of the Internal Revenue Code.

Under the terms of the Trust Deed executed and delivered by decedent on September 27, 1918, the income was payable to decedent's wife for life and thereafter in equal shares to decedent's six children during their respective lives. Upon the death of any child, the share of the income theretofore payable to such deceased child became payable to the surviving children of such deceased child, if any, or if there were no surviving child or children of such deceased child, then to the survivors of decedent's six children or grandchildren, *per stirpes*. The trust was to terminate on the death of the last survivor of decedent's six children, and the corpus would then be distributable *per stirpes* to decedent's grandchildren, if any, then living and the children then living of any deceased grandchild. (App. 17 a-20 a)

The decedent reserved no reversionary or remainder interest to himself in the trust nor any power to alter, amend or revoke the trust. (App. 17 a-21 a) The Trust Deed, however, contained the following provisions:

> "6. The trust may, however, be wholly terminated at any time, or in part from time to time, in the following manner. If all the beneficiaries hereinabove named, that is, my wife and my six children, or said children alone after my wife's death or the survivors of them, shall request a termination in writing directed to the trustees and to me, and I shall in writing delivered to the trustees consent thereto, the trust shall, upon delivery of such request and consent to the trustees, be terminated either wholly or in part, or as to the interest in

whole or in part of any of said beneficiaries, in accordance with such request and consent, and the trust property shall be released in whole or in part accordingly, and the portion so released shall be assigned, transferred and conveyed to the beneficiary or beneficiaries designated in said written request to be his or her absolute property, free and clear of all trusts and conditions; provided, however, that if such termination is made before the death of my wife, the property released shall be equally divided between her and the children, that is, one-half to her and one-half to the children or the child whose portion is released. If after her death, the property released shall go to the children or the said child whose portion is released."

The Trust Deed also contained a spendthrift trust clause as follows:

"7. All payments and transfers to be made hereunder, either of principal or income, shall be made directly to the person or persons named or designated herein as beneficiaries, and to no other person or persons, it being intended that the interests of the beneficiaries shall not be subject to their debts, liabilities, engagements, assignments or transfers, nor liable to any attachment, or execution, or other legal process against them."

On the date of decedent's death, the corpus of the trust had a fair market value of $285,527, and the value of the remainder interests after the lives of decedent's five surviving children who were the life tenants under the trust, was $129,865.67. One of the decedent's children named as a life tenant under such trust and decedent's wife, Jessie B. Thorp, predeceased decedent. (App. 15 a) In addition to five of his children, decedent

was survived by eleven grandchildren. (Exhibit "B" of Motion to Supplement Record on Review)

The beneficiaries of said trust did not, during the period from the date of its creation, September 27, 1918, to the date of decedent's death, December 14, 1942, request a termination as to all or any part of said trust. (App. 15 a)

JURISDICTION.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended, 28 U.S.C. 347(a) and Section 1141 of the Internal Revenue Code, 26 U.S.C. 1141(a).

QUESTIONS PRESENTED.

1. Whether decedent's privilege of consenting, or refusing to consent, to a request of all the life beneficiaries for a termination of the trust is a "power of termination" within the meaning of Section 811(d)(2) of the Internal Revenue Code.

2. Whether the life beneficiaries of the trust had a substantial adverse interest in the transferred property within the meaning of Section 811(d)(2) of the Internal Revenue Code and the Treasury Regulations thereunder (Reg. 105 Sec. 81.20).

3. Whether the Fifth Amendment to the Constitution of the United States forbids retroactive application of Section 811(d)(2) of the Internal Revenue Code to the transfer in this case which was completed in the year 1918.

REASONS RELIED ON FOR THE ALLOWANCE OF THE WRIT.

1. The decision of the Court below is in conflict with applicable decisions of this Court, which hold that retroactive application of the Federal Estate Tax to a transfer in trust, fully executed prior to the enactment of the statute imposing the tax, where the settlor reserves no interest in the transferred property and no power in himself alone to revoke, to alter, to amend, or to terminate the trust, is in derogation of the Fifth Amendment to the Constitution of the United States.

2. The decision of the Court below is in conflict with decisions of the Circuit Courts of Appeals for the First, Second and Sixth Circuits, which hold that if the joinder of any one or more of several beneficiaries of a trust with the settlor is requisite to the effective exercise of a power to revoke, to alter, to amend or to terminate a trust, the value of the corpus of the trust is not includible in the settlor's estate for Federal Estate Tax purposes.

3. The decision of the Court below is in conflict with decisions of the Circuit Courts of Appeals for the Second and Fourth Circuits, which hold that where certain conditions, imposed upon the exercise by a settlor of a power to revoke, to alter, to amend or to terminate a trust, are never fulfilled, no power exists, and the Federal Estate Tax cannot be imposed thereon.

4. The decision of the Court below is in conflict with decisions of this Court and of the Circuit Courts of Appeals for the First and Seventh Circuits, which define "adverse interest" as a beneficial interest in re-

lation to a person or persons whose joinder with the settlor is requisite to the effective exercise of a power to revoke, to alter, to amend or to terminate a trust.

Respectfully submitted,

ESTATE OF CHARLES M. THORP, Deceased,
GOLDIE D. THORP and FIDELITY TRUST COMPANY, Executors,
Petitioners.

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v.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

OPINIONS BELOW.

The Opinion of the Tax Court was entered on November 21, 1946, and is reported in 7 T. C. 921.

The Opinion of the Circuit Court of Appeals was entered on December 2, 1947, and is included in the record, but is not yet officially reported.

JURISDICTION.

The judgment sought to be reviewed is a final judgment of the Circuit Court of Appeals for the Third Circuit, affirming a decision of the Tax Court of the United States. The jurisdiction of this Honorable Court is invoked under Section 240(a) of the Judicial Code, as amended, 28 U.S.C. 347(a) and Section 1141 of the Internal Revenue Code, 26 U.S.C. 1141(a).

STATUTE INVOLVED.

The statute involved is Section 811(d)(2) of the Internal Revenue Code, 26 U.S.C., Section 811(d)(2).

STATEMENT.

The essential facts are summarized in the Petition for Certiorari under the caption "Summary Statement of the Matters Involved" (*supra,* pages 2 to 5).

SPECIFICATION OF ERRORS TO BE URGED.

The Circuit Court of Appeals erred:

1. In holding that the decedent's privilege of consenting to or vetoing a request by beneficiaries for termination of the trust constitutes a power of termination under the provisions of Section 811(d)(2) of the Internal Revenue Code.

2. In holding that such privilege is taxable despite the provisions of the Fifth Amendment to the Constitution of the United States.

3. In failing to hold that a beneficial interest is an adverse interest.

4. In holding that the life beneficiaries of the trust did not have a "substantial adverse interest."

SUMMARY OF ARGUMENT.

The Trust Deed of September 27, 1918, was an irrevocable completed transfer of the trust property, subject only, with respect to certain remainder interests, to revocation upon the contingency of a request by the life beneficiaries and the consent thereto by the decedent in his lifetime. The decedent retained no legal or equitable interest, and he could never at any time revest in himself any interest legal or equitable in the trust property. This Court has held that any attempt to tax the privilege involved in such consent of the decedent in connection with a fully executed transfer prior to 1924 is prevented by the provisions of the Fifth Amendment to the Constitution of the United States. Furthermore, in view of the fact that termination could not be effected except upon the unanimous request of the life beneficiaries, whose interest would be substantially adversely affected by termination, which request was never made, the privilege of the decedent is not a power of termination within the meaning of Section 811(d)(2), under decisions of this Court and of several Circuit Courts of Appeals.

ARGUMENT.

I.

The Decision of the Court Below Is in Conflict With Applicable Decisions of This Court, Which Hold That Retroactive Application of the Federal Estate Tax to a Transfer in Trust Fully Executed Prior to the Enactment of the Statute Imposing the Tax Where the Settlor Reserves No Interest in the Transferred Property and No Power in Himself Alone to Revoke, to Alter, to Amend or to Terminate the Trust, Is in Derogation of the Fifth Amendment to the Constitution of the United States.

Although an argument on the merits may be inappropriate at this stage of the proceedings, some reference to the underlying points of law is essential to a clear exposition of the case. The provisions of Section 811(d)(2) of the Internal Revenue Code. 26 U.S.C. § 811(d)(2), the history thereof and the Treasury Regulations thereunder must necessarily be considered.

Section 811(d)(2) provides:

"Sec. 811 Gross Estate

"The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—

* * * * * * *

"(d) Revocable Transfers—

* * * * * * *

"(2) Transfers on or prior to June 22, 1936. To the extent of any interest therein of which the decedent has at any time made a transfer, by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power, either by the decedent alone or in conjunction with any other person, to alter, amend, or revoke, or where the decedent relinquished any such power in contemplation of his death, except in case of a bona fide sale for an adequate and full consideration in money or money's worth. Except in the case of transfers made after June 22, 1936, no interest of the decedent of which he has made a transfer shall be included in the gross estate under paragraph (1) unless it is includible under this paragraph."

The Regulations of the Commissioner of Internal Revenue contain, *inter alia,* the following provisions with respect to Section 811(d)(2):

"Reg. 105, Sec. 81.20. *Transfers with power to change the enjoyment.*—(a) *Transfers included.*—Subsection (d) of section 811 embraces a transfer by trust or otherwise (if not amounting to a bona fide sale for an adequate and full consideration in money or money's worth) when at the time of decedent's death the enjoyment of the transferred property, or some part thereof or interest therein, was subject to any change through a power exercisable either by the decedent alone, or by him in conjunction with some other person or persons, to alter, or amend, or revoke, or terminate.

* * * * * * *

"(b) Taxability.—The property or *any* interest therein transferred as described in subsection (a)

shall be included in the gross estate if it comes within any one of the following paragraphs:

"(1) *If the transfer was made prior to the enactment of the Revenue Act of 1924 (4:01 p. m., eastern standard time, June 2, 1924)* and the power was reserved at the time of the transfer and was exercisable by the decedent alone or in conjunction with a person or persons having no substantial adverse interest or interests in the transferred property, or if exercisable in conjunction with a person having a substantial adverse interest or with several persons some or all of whom held such an adverse interest, then to the extent of any interest or interests held by a person or persons not required to join in the exercise of the power and to the extent of any adverse interest which was not substantial.

"(2) If the transfer was made after the enactment of the Revenue Act of 1924 (4:01 p. m., eastern standard time, June 2, 1924) and before the amendment of the subdivision by the Revenue Act of 1936 became effective (June 23, 1936), and the power was reserved at the time of the transfer and was exercisable by the decedent alone or in conjunction with a person or persons either having or not having a substantial adverse interest or interests in the transferred property, or in conjunction with persons one or more of whom had and one or more of whom had not such an adverse interest."

Section 811(d)(2) of the Internal Revenue Code was adopted in 1936, amending Section 302(d) of the 1926 Revenue Act. This latter was a substantial reenactment of Section 302(d) of the Revenue Act of 1924. Prior to the Revenue Act of 1924, there had been no provision in any Revenue Act expressly covering cases

of *inter vivos* transfers where the grantor reserved a power exercisable by himself alone or jointly with another person to alter, amend or revoke such transfers.

We have, therefore, this situation: On September 27, 1918, decedent made a completed transfer in trust, retaining no beneficial interest and no power to revest in himself any such interest, but simply reserving to himself the privilege of consenting, or refusing to consent, to a termination of the trust, if the life beneficiaries should unanimously request termination. That transfer was not taxable under any Federal Estate tax statute in force on September 27, 1918.

That the decedent had made a completed transfer in 1918 is beyond peradventure of doubt under the decisions of the Supreme Court of Pennsylvania, of which state decedent was a resident on the date of execution of the Trust Deed (App. 17 a) as well as at the time of his death (App. 14 a). See *Glosser Trust,* 355 Pa. 210 (1946), which holds that a transfer in trust is a perfected gift *inter vivos* where the donor reserves no beneficial interest and no power to reassert dominion over the property. Under *Helvering v. Stuart,* 317 U. S. 154, 63 S. Ct. 140 (1942) the Pennsylvania decisions are controlling on this phase of the matter.

The Federal Estate Tax is an excise tax on the privilege of transferring property at the time of death. Here nothing passed from the decedent at the time of his death, he having divested himself absolutely of all title to the trust property on the date of the Trust Deed, viz., September 17, 1918. At that time, as stated hereinabove, there was no existing legislation expressly taxing a reserved power of termination exercisable only in con-

junction with some of the beneficiaries of the trust. Under these circumstances, the so-called "power" is not subject to tax under a subsequently enacted statute, because of the provisions of the Fifth Amendment to the Constitution of the United States.

This Court so held in unmistakable language in *Helvering v. Helmholz,* 296 U. S. 93, 56 S. Ct. 68 (1935). That case involved a trust created in 1918, and the provisions of the trust contained a reservation in the grantor to terminate the trust in conjunction with other persons. This Court said, page 97:

> "Another and more serious objection to the application of Section 302(d) in the present instance is its retroactive operation. The transfer was complete at the time of the creation of the trust. There remained no interest in the grantor. She reserved no power in herself alone to revoke, to alter, or to amend. Under the Revenue Act then in force, the transfer was not taxable as intended to take effect in possession or in enjoyment at her death. Reinecke v. Northern Trust Company, 278 U. S. 339, 49 S. Ct. 123, 73 L. Ed. 410, 66 A.L.R. 397. If Section 302(d) of the Act of 1926 could fairly be considered as intended to apply in the instant case, its operation would violate the Fifth Amendment. Nichols v. Coolidge, 274 U. S. 531, 47 S. Ct. 710, 71 L. Ed. 1184, 52 A.L.R. 1081."

Appended to the opinion of the Court is this notation, which has reference to the subject matter of the foregoing quotation, page 98:

> "Mr Justice Brandeis, Mr. Justice Stone and Mr. Justice Cardozo concur in the result on the ground last stated in the opinion."

Here we have the unanimous decision of this Court, as then constituted, to the effect that a power of termination in a trust created prior to 1924, not exercisable by the grantor alone, cannot be taxed retroactively.

On the same day and on a similar state of facts, in *White v. Poor,* 296 U. S. 98, 56 S. Ct. 66 (1935), this Court repeated its ruling in *Helvering v. Helmholz,* using this language at page 102:

> "What has been said in No. 14 (Helvering v. Helmholz) requires a ruling that the section, if held to apply to this transfer, offends the due process clause of the Fifth Amendment."

Similarly, there was appended to the decision this notation:

> "Mr. Justice Brandeis, Mr. Justice Stone and Mr. Justice Cardozo concur in the result."

We assert, without fear of successful contradiction, that this Court has never departed from that rule. Certainly, the principle laid down in *Commissioner of Internal Revenue v. Holmes' Estate,* 326 U. S. 480, 66 S. Ct. 257 (1946), is not inconsistent therewith. That case involved a trust *created in the year 1935,* which could be terminated *at the sole discretion of the settlor.* These factors differentiate the case entirely from the instant case. This Court held (Mr. Justice Douglas dissenting), that a power of termination was included within the meaning of the phrase "power to amend, alter or revoke," and that, therefore, Section 302(d) was applicable to a trust created after adoption of the Revenue Act of 1924 but prior to the amendment of 1936, when, for the first time, the word "terminate" was added and

made specifically applicable to subsequent transfers. By no stretch of construction can it be said that the ruling of the *Holmes* case applies to the instant case or overrules the principle of *Helvering v. Helmholz, supra,* and *White v. Poor, supra,* from which we have quoted, nor did that case purport so to do by any language used therein.

We anticipate reliance by the respondent on the case of *The Union Trust Company of Pittsburgh v. Driscoll,* 138 F. 2d 152 (CCA 3, 1943), in which this Court denied certiorari, 321 U. S. 764, 64 S. Ct., 521 (1944). That case involved an oral trust created by the decedent in 1918, and reduced to writing in 1931, under which the decedent and her husband were trustees for the benefit of certain nephews and nieces. There was reserved to such trustees the absolute and uncontrolled right to vary the relative proportions to be distributed to the beneficiaries. The Circuit Court of Appeals for the Third Circuit held that the value of the trust was taxable as part of the decedent's gross estate. That case differs from the cases of *Helvering v. Helmholz* and *White v. Poor, supra,* in that no person with a beneficial interest in the trust was required to join in the exercise of the power of the trustees to vary the relative proportions of distributions.

We submit, therefore, that a refusal of certiorari in the *Driscoll* case has no significance with respect to the issue in the instant case where the settlor was powerless to do anything unless and until all of the life beneficiaries of the trust should join in a request for termination, and then he could only consent to or, by withholding consent, prevent a termination.

The decision of the Court below is in conflict on another point with the decision in *White v. Poor, supra,* in which the power of termination was vested in three trustees, one of whom was a beneficiary to the extent of one-sixth of the income of the trust. Two other beneficiaries holding similar interests were not required to join in the termination. This Court held that, under those circumstances, the trust could not be included in the grantor's estate. In other words the fact that not *all* of the beneficiaries of the trust are required to consent to termination is of no significance. That, of course, is precisely the situation in the case at bar in which termination could have been effected without the consent of the holders of the remainder interests.

The decision of the Court below is also in conflict with the decision of this Court in *Reinecke v. Northern Trust Company,* 278 U. S. 339, 49 S. Ct. 123 (1929) involving seven separate trusts and holding non-taxable in the estate of the grantor the value of five of the trusts, the provisions of each of which could be amended, but only by joint action of the grantor and the life beneficiary of each such trust respectively. The holders of the remainder interests there, as in the case at bar, were not required to join in the amendment of any of those five trusts.

II.

The Decision of the Court Below Is in Conflict With Decisions of the Circuit Courts of Appeals for the First, Second and Sixth Circuits, Which Hold That if the Joinder of Any One or More of Several Beneficiaries of a Trust with the Settlor Is Requisite to the Effective Exercise of a Power to Revoke, to Alter, to Amend or to Terminate the Trust, the Value of the Corpus of the Trust Is Not Includible in the Settlor's Estate for Federal Estate Tax Purposes.

In *Commissioner of Internal Revenue v. Kaplan,* 102 F. 2d 329 (CCA 1, 1939) affirming B.T.A. Memo. Dec. Docket No. 81780, entered March 4, 1938 (CCH Dec. 9975-J), the facts were as follows. Decedent created a trust in 1923, with income payable to his wife during her life and then to himself, if he survived her. Upon the death of the survivor, the corpus was to be divided equally among their children and the issue of such children. The trust could be amended or revoked by the decedent with his wife's consent. The remaindermen were not required to join in the amendment or revocation. The settlor died in 1933, survived by his wife and their children. The Commissioner made no attempt to include the value of the life estate in the trust in decedent's gross estate, but determined a deficiency based on including the value of the remainders. The Board of Tax Appeals held that no part of the corpus could be included under Section 302(d) of the Revenue Act of 1926 because the trust had been created prior to enactment of the Revenue Act of 1924 and the reserved power to amend or revoke the trust could be exercised only by joint action of the decedent and his wife. The Commissioner's argument with respect to

the inclusion of the value of the remainder interests was the same as in the case at bar, viz., that since no person who had a remainder interest was required to join in the destruction of such remainders, the power to amend or revoke such remainders was one which could be exercised by decedent alone. The Board of Tax Appeals disagreed with that argument and held that the remainders could not be included, and the Circuit Court of Appeals for the First Circuit affirmed the decision of the Board of Tax Appeals. *Obviously, this case cannot be reconciled with the decision of the Court below.*

In *Bryant v. Commissioner of Internal Revenue,* 104 F. 2d 1011 (CCA 2, 1939), affirmed sub nom. *Bryant v. Helvering,* 309 U. S. 106, 60 S. Ct. 444 (1940), a trust was created in 1917 and the income thereof was made payable to decedent's wife for life, then to decedent if living, and upon the survivor's death, the corpus was payable to decedent's estate. The trust could be modified or revoked by joint action of decedent and his wife during their joint lives or by the survivor of them alone. Decedent died in 1930, survived by his wife. The Commissioner claimed that the entire trust was includible in decedent's gross estate either under Section 302(c) or 302(d) of the revenue Act of 1926. The Tax Court (36 B.T.A. 669 (1937)) agreed with the Commissioner's contention with respect to Section 302(c) but pointed out that under the doctrine of *Helvering v. Helmholz, supra,* and *White v. Poor, supra,* no part of the corpus could be included under Section 302(d) of the 1926 Act, because the trust was created prior to the Revenue Act of 1924 and could be altered, amended or revoked only if decedent's wife (who was the life beneficiary but had

no interest in the remainder) joined in such action with the decedent. The Circuit Court of Appeals for the Second Circuit affirmed "Per Curiam." This Court likewise affirmed the Tax Court's ruling respecting Section 302(c), but did not dispute the correctness of the Tax Court's holding with respect to Section 302 (d).

There is another decision of the Circuit Court of Appeals for the Second Circuit, which is also in direct conflict with the decision of the Court below, viz., *Mackay v. Commissioner,* 94 F. 2d 558 (CCA 2, 1938). That case involved six trusts created by the decedent in 1919, the income being payable to certain initial and secondary life beneficiaries with remainder over to Mackay, if living, otherwise to the children of Mackay. The trusts could be amended or revoked by joint action of the decedent and the trustees, of which Mackay at all times until decedent's death was one. Decedent died in 1928. The Commissioner asserted a deficiency in estate tax based on including in decedent's gross estate the value of the corpora of such six trusts under Section 302(d) of the Revenue Act of 1926.

The Board of Tax Appeals (33 B.T.A. 765 (1935)) held that the value of the remainders, was not includible in the gross estate, in that Section 302(d) did not apply as the trusts were created before enactment of the 1924 Revenue Act, citing *Nichols v. Coolidge,* 274 U. S. 531, 47 S. Ct. 710 (1927). The Board held, however, that the power of amendment and revocation, in which no life beneficiary was required to join, brought the value of the life estates within Section 302(d) of the 1926 Revenue Act, relying on *Reinecke v. Northern Trust Company, supra,* as to the taxability of two of the seven

trusts held to be taxable in that case. The Circuit Court of Appeals for the Second Circuit reversed the Board of Tax Appeals and held that, since the consent of Mackay, one of the remaindermen, was required to any revocation of the trust or amendment of any life interests, the principle followed in *Reinecke v. Northern Trust Company, supra,* to support the taxing of two of the trusts there involved was not applicable, and, on the other hand, that the principle in the *Reinecke* case, under which five of the trusts were held not taxable, applied with equal force in the *Mackay* case and prevented inclusion in decedent's gross estate of any value in respect of such trusts.

The case at bar differs from the *Mackay* case only as to the group whose consent to termination was required. In the *Mackay* case, the life beneficiaries and secondary remaindermen were not required to consent, whereas in the case at bar, none of the remaindermen was required to consent. Plainly, however, the rule of the *Mackay* case that neither the life estates nor the remainder interests could be taxed is equally applicable to the case at bar and makes the decision conflict with the decision of the Court below.

In *Commissioner of Internal Revenue v. Hallock,* 102 F. 2d. 1 (CCA 6, 1939), reversed sub nom. *Helvering v. Hallock,* 309 U. S. 106, 60 S. Ct. 444 (1940), the Circuit Court of Appeals for the Sixth Circuit had before it a trust created in 1919 providing that the income should be paid to decedent's divorced wife and upon her death that the corpus should be distributed to the decedent, if he survived his wife, otherwise to his children. The trust could be altered, modified, terminated or cancelled by the joint action of the decedent and his wife. The

Commissioner sought to include the entire trust in decedent's gross estate under Section 302(c) of the Revenue Act of 1926 as intended to take effect in possession or enjoyment at or after death and under Section 302(d) of the same Act because of the reservation aforesaid. The Board of Tax Appeals (34 B.T.A. 575 (1936)) held that the Commissioner's claim under Section 302(d) of the 1926 Act was untenable because of the decisions of this Court in *Helvering v. Helmholz, supra,* and *White v. Poor, supra,* and that the trust was not includible under Section 302(c) of the 1926 Act, relying upon *Helvering v. St. Louis Union Trust Company,* 296 U. S. 39, 56 S. Ct. 74 (1935). The Circuit Court of Appeals for the Sixth Circuit affirmed as to the application of Section 302(c), no issue being raised as to Section 302(d). This Court on appeal (309 U. S. 106, 60 S. Ct. 444 (1940)) held that Section 302(c) was applicable, overruling *Helvering v. St. Louis Union Trust Company, supra,* but not questioning the correctness of the decision as to non-application of Section 302(d).

III.

The Decision of the Court Below Is in Conflict With Decisions of the Circuit Courts of Appeals for the Second and Fourth Circuits, Which Hold That, Where Certain Conditions, Imposed Upon the Exercise by a Settlor of a Power to Revoke, to Alter, to Amend or to Terminate a Trust, Are Never Fulfilled, No Power Exists, and the Federal Estate Tax Cannot Be Imposed Thereon.

Under the provisions of paragraph 6 of the Trust Deed quoted in the Petition for Certiorari at page 3 *supra,* termination of the trust could not be initiated by the decedent. The exercise of his privilege of consenting, or refusing to consent, to a termination was completely dependent upon the submission to the trustees and to him by all of the life beneficiaries, or their survivors, of a written request for termination. The record shows (App. 15 a) that no such request for termination of the trust, in whole or in part, was ever made. Therefore, for all practical purposes, the decedent's privilege of consenting to or refusing to consent to termination never came into existence. Moreover, such a privilege, based upon a condition that is not fulfilled, is not a power of termination within the meaning of Section 811 (d) (2) of the Internal Revenue Code under decisions of the Circuit Courts of Appeals for the Second and Fourth Circuits.

In *Commissioner v. Flanders, et al.,* 111 F. 2d 117 (CCA 2, 1940) affirming B.T.A. Memo. Opinion No. 88787, entered February 17, 1939 (CCH Dec. 10607-C), the facts were as follows: The trust was created by

decedent, Clark, in 1910. The income thereof was payable to the grantor for life with remainders to the grantor's issue and in default of issue to grantor's brothers or their issue. At the grantor's death, one of his three brothers was to become one of the trustees. The trust instrument authorized the trustees, in case an emergency arose which, in the exercise by the trustees of a sound discretion and judgment, rendered it advisable, to sell the securities forming the corpus of the trust, provided the grantor before the making of any such sale consented thereto. Upon any such sale the trust terminated as to the proceeds of the securities sold, which proceeds reverted free of the trust to the grantor. No emergency justifying a sale arose at any time after the trust was created and consequently the trustees had no occasion to exercise any judgment as to the advisability of any sale, nor was the grantor's consent to any sale ever invoked. The Board of Tax Appeals held that the right to consent was not a power existing in the grantor at the time of his death within the meaning of Section 302(d) of the 1926 Revenue Act because (a) no emergency had arisen and (b) the trustees had not determined the advisability of selling any of the securities. The Circuit Court of Appeals for the Second Circuit affirmed the Board of Tax Appeals in so holding.

In *Tait v. Safe Deposit and Trust Company of Baltimore,* 74 F. 2d 851 (CCA 4, 1935), the grantor reserved a power to alter trust distributions payable after his death, except that he could not affect in any way the remainder interest of his wife in one-half of the corpus. It was argued that if the wife had predeceased him, which had not occurred, the wife's interest would become subject to his reserved power and consequently the

reserved power could be held to be within Section 302(d) of the 1926 Revenue Act. The Circuit Court of Appeals for the Fourth Circuit held, however, that the grantor's power with respect to his wife's interest was contingent upon his surviving his wife, and, since the wife was living at the time of his death, it was not a power within Section 302(d) of the 1926 Revenue Act.

The Court below rejects the doctrine of these cases (see pages 3 and 4 of its Opinion) and holds that it is immaterial as to who is privileged to take the initial step in termination. The decision of the Court below cannot be reconciled with the above decisions of the Second and Fourth Circuit Courts of Appeals.

The decision of the Tax Court in the instant case (7 T. C. 921) is directly opposed to its earlier decision in *Orrin G. Wood,* 40 B.T.A. 905 (1939), in which it held that a grantor's reserved power to veto any change that the trustees might make in the beneficial interests was not a power to alter, amend or revoke the trust. That the gift tax and not the Estate tax was there involved is of no significance. The Tax Court in no way reconciles these diverse decisions. Its opinion in the instant case is analyzed and severely criticised in a Note in the Boston University Law Review, Vol. XXVI, No. 4 (November 1946), pages 524-5.

IV.

The Decision of the Court Below Is in Conflict With Decisions of This Court and Decisions of the Circuit Courts of Appeals for the First and Seventh Circuits, Which Define "Adverse Interest" as a Beneficial Interest in Relation to a Person or Persons Whose Joinder With the Settlor Is Requisite to the Effective Exercise of a Power to Revoke, to Alter, to Amend or to Terminate a Trust.

Treasury Regulations 105, Section 81.20(b)(1), quoted supra at page 15, predicate taxability in the case of a transfer prior to the enactment of the Revenue Act of 1924 on the reservation of a power exercisable by decedent alone or in conjunction with a person or persons "having no substantial adverse interest or interests in the property transferred."

In *Reinecke v. Northern Trust Company, supra,* this Court said at page 346:

> "Since the power to revoke or alter was dependent on the consent of the one entitled *to the beneficial, and consequently adverse interest,* the trust, for all practical purposes, had passed as completely from any control by decedent which might inure to his benefit as if the gift had been absolute." (Emphasis Ours)

In other words a beneficial interest is *ipso facto* an adverse interest.

The Court below at page 5 of its Opinion rejects this principle and adopts as a test whether or not the change which would result from the exercise of the

power is adverse to the holder of the beneficial interest whose consent to such exercise is required. The theory of the Court below seems to be that, if the exercise of the power would result in a benefit to the person whose joinder in its exercise is required, then such a person is not to be characterized as having a substantial adverse interest in the property transferred.

We submit that that is a completely erroneous construction of the Regulations. To arrive at that conclusion, the language used, viz., "having no substantial adverse interest or interests in the property transferred," must be twisted into "having no substantial interest adverse to the effect of the exercise of the power." Plainly, what was intended by the Regulations was that the person required to join with the grantor in the exercise of the power must have no interest in the transferred property adverse to the grantor, as, for example, a trustee. The word "adverse" was not intended to relate to the effect of the exercise of the power. Clearly, therefore, the decision of the Court below on this point is in conflict with the holding of this Court in *Reinecke v. Northern Trust Company, supra.*

There are several decisions of Circuit Courts of Appeals which likewise cannot be reconciled with the decision of the Court below. In *Commissioner v. Prouty,* 115 F. 2d. 331 (CCA 1) (1940), the Circuit Court of Appeals for the First Circuit, referring to the similar language of Section 501 of the Revenue Act of 1932, 47 Stat. 245, as amended by Section 511 of the Revenue Act of 1934, 48 Stat. 758, 26 U.S.C.A., pages 580, 769, imposing gift taxes, says, at page 335:

"but we think the phrase 'substantial adverse inter-

> est' • • • means a direct legal or equitable interest in the trust property."

This language was quoted with approval by the same Court in *Flood v. United States,* 133 F. 2d 173, 177, (CCA 1) (1943), a case involving the Revenue Acts of 1936 and 1938, 26 U.S.C., §§166, 167, imposing income taxes on trust income.

In *Commissioner v. Betts,* 123 F. 2d 534 (CCA 7, 1941), the Circuit Court of Appeals for the Seventh Circuit, in reference to a person holding a "substantial adverse interest," within the meaning of the Revenue Acts of 1934 and 1936, 26 U.S.C., §166, imposing income taxes on trust income, says:

> "What Congress had in mind evidently was such a person as has a vested right under a trust agreement to insist upon its performance and cannot be compelled to surrender the same."

The decision in *Mackay v. Commissioner, supra,* is substantially to the same effect. There the Circuit Court of Appeals for the Second Circuit pointed out that the power of amendment might be exercised in such a way as to be beneficial to that one, of several remaindermen, whose consent to amendment was required. Conceivably also it might be exercised to his detriment. The Court refused to speculate as to whether the possible benefits outweighed the possible adverse results of amendment and simply held the corpus of the trusts not includible in the grantor's estate for Federal Estate Tax purposes. The Court's conclusion is virtually an adoption of the simple rule promulgated by this Court in *Reinecke v. Northern Trust Company, supra,* viz., *a beneficial interest is an adverse interest.*

The Court below reasoned in a precisely opposite manner. Conceding the possibility of expansion of the interests of the life beneficiaries, which would be destroyed by the termination of the trust, nevertheless the Court says that "the possibility of such expansion does not compel the conclusion that their position was 'substantially adverse'." (See Opinion, top of page 5)

The confusion in the decisions as to what constitutes "substantial adverse interest" under Section 811 (d) (2) and the regulations thereunder plainly appears from the exhaustive discussion thereof in Mertens "The Law of Federal Income Taxation" (1942), Vol. 6, Section 37.13 and the 1947 Cumulative Pocket Supplement thereto. It is respectfully submitted that this learned Court should clear up this confusion.

We fully appreciate that it is not appropriate at this stage of the proceeding to discuss at length the merits of the conclusion of the Court below that the life beneficiaries of the instant trust had no substantially adverse interest against its termination. We do not concede the correctness of that conclusion or its finality upon this Court under the rule of *Commissioner v. Scottish American Co.*, 323 U. S. 119, 65 S. Ct. 169, cited by the Court below (Opinion, page 4), a case in which the Tax Court's conclusion was held to have been based upon substantial evidence. In the case at bar the facts were stipulated (App. 14 a *et seq.*). Moreover a correct determination of the question of "substantial adverse interest" involves simply the construction of paragraphs 5 and 6 of the Trust Deed (App. 18 a, 19 a); in other words, it is purely a question of law, involving no fact determination whatever.

A brief statement as to the effect of termination on the interests of the life beneficiaries: As a result of the

decease of one of the life beneficiaries without issue (Exhibit "B" of Motion to Supplement the Record; Opinion of the Court below, page 3) the five surviving life beneficiaries are now each enjoying one-fifth of the income rather than the one-sixth thereof received by each prior to that event. Termination of the trust prior to that event would have destroyed the possibility of that expansion as well as the possibility of subsequent expansion into a larger fractional interest in the trust income. Moreover, the spendthrift trust provisions of the Trust Deed quoted in the Petition for Certiorari, page 4, *supra,* represent a distinct advantage to the life beneficiaries which a termination of the trust would have eliminated.

We submit that these are substantial interests which would be adversely affected by a termination and that, the holding of the Court below to the contrary notwithstanding, they should compel the conclusion that the position of the life beneficiaries was substantially adverse, whether or not the rule of *Reinecke v. Northern Trust Co., supra,* page 29, is applied.

Respectfully submitted,

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